FPI BOARD OF DIRECTORS MEETING
September 2, 2015
Washington, D.C.

A meeting of the Federal Prison Industries (FPI) Board of Directors was held at the Department of Justice (DOJ), Washington, D.C., Wednesday, September 2, 2015.

IN ATTENDANCE:

David Spears, Chairman
Don Elliott, Member
Frank Gale, Member
Audrey Roberts, Member
Lee J. Lofthus, Member

QUORUM: A quorum was present.

ALSO IN ATTENDANCE:

Charles E. Samuels, Jr., Director, Bureau of Prisons
Chief Executive Officer, FPI
Mary M. Mitchell, Assistant Director, IEVT
Chief Operating Officer, FPI
Judi Simon Garrett, Assistant Director, IPPA
Phil Sibal, Senior Deputy Assistant Director, IEVT
Ken Yeich, Deputy Assistant Director, IEVT
Marianne Cantwell, General Counsel, IEVT
Brad Beus, Chief Financial Officer, FPI
Robert Grieser, Chief, Marketing, Research
& Corporate Support, FPI
Christian Burch, Executive Assistant, IEVT
For McKinsey Presentation only:
Scott Rutherford, Director, McKinsey&Company
Ian Schillinger, Associate Principal, McKinsey&Company

Chairman Spears called the meeting to order at 7:53 a.m. and thanked Mr. Lofthus and his staff for hosting the meeting.

I. Approval of the May 28, 2015 Meeting Minutes

The Board of Directors considered the draft minutes from the May 28, 2015 meeting conducted at FCI El Reno, El Reno, OK. The Board voted unanimously to accept the minutes as presented. Chairman Spears reiterated that future meeting minutes should capture more of the dialogue involved during meetings. All other members concurred with this request. Specifically, Mr. Gale noted the importance of capturing responses of the Board members, particularly for motions and action items.

Mr. Lofthus inquired for specifics regarding product lines that were struggling. He further added that the Board needed to visit factories/operations with the most challenging issues. Director Samuels highlighted that executive staff are on travel status frequently, which presents scheduling challenges for visits to specific factories. He added that some of the factory challenges stemmed from staff retention within FPI. He noted that staff often seek opportunities in other areas of the agency due to the uncertainty of FPI's long-term sustainability.

Mr. Spears requested that Ms. Mitchell consult with her executive staff team to determine which facilities would be best for upcoming visits/tours. Mr. Lofthus noted that the previously discussed dates of January 27 and 28, 2016 for the next Board meeting might present issues due to the President's budget rollout the week after. Mr. Spears recommended the Board consider the week of January 19, 2016.

The Board discussed the date of its next meeting and proposed locations where factories with diverse operations could be toured. Ms. Mitchell recommended January 27 or 28 for the meeting and FCI Jessup or FCI Bastrop as locations. Subsequently, the date of January 19, 2016 was approved for the next meeting. Mr. Spears noted the importance of selecting locations where travel costs would be minimized to the maximum extent possible. He also noted that there had been a high frequency of meetings held in Washington, D.C. as compared to previous years. Additionally, he suggested that interim conference calls be held between Board meetings to better keep Board members abreast of FPI's progress and financial status.

Ms. Mitchell clarified with Mr. Spears whether he was suggesting that Board meetings be held via teleconference in lieu of quarterly meetings or held in addition to regularly scheduled meetings. Several members of the Board confirmed their recommendations to hold teleconferences in between regularly scheduled in-person meetings.

II. Chief Executive Officer's Report

Director Samuels thanked Mr. Lofthus for hosting the Board meeting and thanked Board members for their attendance and continued support of FPI. He stated the following about his upcoming retirement: "I am sure you have heard, I announced my retirement, and will be stepping down at the beginning of next year. So, this is probably my last meeting with all of you."

"Leaving the Bureau will not be easy. I have truly enjoyed my career. From when I started as a correctional officer at FCI Talladega in 1988, until today, I can truly say I have had 27 amazing years. But it's time for me to step aside and let someone else continue to move the agency forward."

Director Samuels spoke about President Obama's visit to FCI El Reno in July. He noted that this was the first time a sitting United States President had ever visited a federal prison. Director Samuels noted that the President sat down and spoke with six inmates who shared their stories about how they ended up in prison, and many spoke about how the Bureau has positively impacted their lives. He stated that one inmate spoke positively about FPI, expressing to the President that working in FPI allowed him to buy a home for his mother. Director Samuels further commented that their stories made a positive impression, and he believes they helped us promote the benefits of FPI and other evidence-based programs to a national audience.

Director Samuels informed the Board that the President's visit was captured in a documentary being produced for HBO by Vice Productions and is scheduled to air on September 27. He added that he was uncertain about what to expect from the documentary, yet cautiously optimistic about the portrayal of the Bureau and FPI.

Director Samuels again expressed his appreciation for the efforts of this Board and its support for the many FPI initiatives that have been collectively pursued during his tenure. He further commented that each Board member had demonstrated an immense commitment to FPI and the Bureau, all of which have directly contributed to sustain this vital program and the corporation. He stated, "I know all of you believe in FPI, and the benefits it provides, and I am confident in saying it is one of the Bureau's most important reentry programs."

Director Samuels added that he will truly miss being a part of this great agency. Director Samuels commented, "I have no doubt this Board will continue to advance the mission of Federal Prison Industries on the corporate level and as a valuable resource to the Bureau, to the inmates and to the Nation."

Director Samuels noted the collective efforts that had been made for the agency and FPI, specifically through Union negotiations. He further added that such efforts had revitalized the agency's relationship with the Union. He noted that the agency had finalized approximately 90 policies in less than two years, which was an unprecedented accomplishment. He added that this was all accomplished despite a number of significant executive staff retirements.

Director Samuels noted he was looking forward to hearing from the Deputy Attorney General later in the morning and expects a full agenda.

III. Chief Financial Officer's Report:

Mr. Beus, Chief Financial Officer, provided the financial update and stated that Sales were 29% above plan through July 2015, $375.1 million versus a plan of $290.6 million. Factory earnings were 104% above plan, $24.9 million versus $12.6 million.

Mr. Beus noted that factory overhead (not presented) was 5.3% above plan, $118.4 million versus $112.5 million. However, this amount includes $5.6 million that is attributed to the Agribusiness Group, which was not part of the original plan.

Mr. Beus informed the Board that General and Administrative Expenses (G&A) were 2.6% below plan, $43.2 million versus $44.4 million. He also stated that net loss from the beginning of the fiscal year was $8.7 million versus a planned loss of $29.7 million. In the 1st Quarter FPI received $6.2 million of non-cash assets from the Bureau of Prisons when farm operations were transferred. This transfer originally increased other income; however, this transaction will be reclassified and it will instead increase capital and thus reduce income by $6.2 million.

Mr. Beus noted that overall cash as of July 31, 2015, was $227.4 million or $42.2 million above the plan of $185.2 million. Since the end of the 2nd Quarter FPI cash has decreased by $13 million due to the decrease in operating cash. Accounts Receivable (AR) increased from April 2015 to July 2015; however, AR over 60 days decreased by 30.7%. This increase in AR is directly related to higher revenues in July.

Mr. Beus highlighted that as of July 31, 2015, inventory was $136.6 million versus a plan of $64.5. The variance is made up primarily of $46.7 million related to vehicle buys and $16.6 million associated with multiple element agreement (MEA) orders which require customer acceptance. These orders are primarily systems furniture orders. The customer must accept these installations 100% before invoicing.

Mr. Beus shared with the Board the following revised plan involving several of the business groups:

The 4th Quarter Sales projections for the Recycling Business Group are consistent with original planned levels. Sales for the Office Furniture Business Group and the Services Business Group are projected to decline from the original plan; however, both Business Groups will exceed annual objectives. Sales projections for the Clothing and Textiles and Electronics Business Groups are expected to be above plan for the 4th Quarter (Clothing and Textiles $24.1 million above plan and Electronics $7.7 million above plan). The Agribusiness Group is projected to generate $6 million in overall sales for Fiscal Year 2015,this amount was not part of the original plan. The revised plan reflects a $94 million increase in sales to $448.7 million versus a plan of $354.9 million. The revised plan reflects a $10.9 million increase in factory earnings and a $1.3 million decrease in General and Administrative Expenses. The revised plan for FPI cash at the time of the May Board of Directors meeting was $188 million compared to the $184 million for the period ending July 2015. FPI cash is projected to increase to $212 million by the end of the fiscal year. Factors contributing to the increase in FPI cash are a reduction in inventory of $13 million and a reduction in accounts receivable of $3 million.

Mr. Beus covered with the Board the following Fiscal Year 2016 Operating Plan:

FPI Sales are projected to drop by $42 million during FY16 versus the FY15 revised plan. Factory earnings are also projected to drop; however, despite lower sales volume profit margin at the factory level will be consistent with FY15, approximately 6%. This is attributed to consolidation of capacity from mothballing factories. Factory earnings are projected to be $24 million versus $27 million revised FY15 projections. General and Administrative Expenses will increase $1.1 million versus the revised FY15 projections. Total losses for FY16 are projected to be $23 million versus projected losses for FY15 of $15 million; however, FY15 revised projections include other income of $6.2 million from the farm transfer, which will be reclassified into capital and will not be reported as part of income. The FY16 Operating Plan will result in a projected decline in cash of $11.8 million.

Mr. Elliott asked Mr. Beus how the assumptions had been made. Mr. Beus stated that a number of factors were involved such as, business group projections, inventory increases and decreases, and accounts receivable collections increases and decreases. Ms. Mitchell added that she would cover specific assumptions during her Chief Operating Officer's report.

Mr. Elliott asked Mr. Beus what actions had been taken to monitor variances. Mr. Beus noted that he had used earnings levels and margins to monitor this, however, levels can vary. He further stated that he did not predict, for example, repatriation in these calculations. Repatriation is primarily contract manufacturing where we are selling our labor and overhead therefore the margins are lower.

Mr. Beus noted that recent estimates were good, but that it is difficult to project inventory fluctuations.

Mr. Spears stated that he had spent some time with Ms. Mitchell prior to the meeting to discuss the differences in the current financial standing and the amount that had been allotted for McKinsey thus far ($3.5 million).

Mr. Lofthus asked Mr. Beus about projected audit costs and why the projected amount was lower for FY16 than it was for FY15. Mr. Beus explained that there were FPI staffing resources built into this cost center that do not work on the Audit full time and therefore costs were shifted to better reflect the budget. Mr. Beus also noted that they made a three-year comparison to establish the budgeted figure. Mr. Beus would also verify that calculations were made based on the Department and the Bureau of Prisons absorbing some of these costs.

Mr. Elliott asked Mr. Beus why there was a $400,000 reduction in New Business Development (NBD). Mr. Beus explained that this was for resource shifting which was not represented in the budget. Ms. Mitchell noted some vacancies within NBD which may result in salary savings that could impact projections also.

Mr. Elliott asked why there was a reduction in the Quality and Continuous Improvement Branch's (QCIB) budget of $1.4 million. Ms. Mitchell explained that after much consideration, Lean Six Sigma Green Belt training had been reduced. Mr. Elliott asked how we were adequately measuring quality and training, further noting that FPI has to substantiate actions. Ms. Mitchell advised the Board of the validation process used last year, further addressing the decision not to fill Black Belt training positions last year and discontinue Green Belt training this year.

Mr. Elliott asked if any audit concerns had been raised. Mr. Beus noted that only one No Findings Report (NFR) was issued, however it was of minimal concern.

Mr. Spears asked Mr. Beus about FPI's projected numbers and how many jobs we anticipate. He also asked "where is FPI headed?" Mr. Elliott stated to everyone in the room that he would like everyone's commitment on "measuring" quality.

IV. McKinsey Update

Before the McKinsey group began their briefing to the Board, Mr. Lofthus asked of FPI management what makes a profit, and when FPI sells an item (a shirt for example), does if we know how much profit is made per shirt? Ms. Mitchell responded to Mr. Lofthus' question by stating: FPI recently conducted numerous time studies, held training for staff in procurement procedures, is moving skilled staff into temporary positions, is identifying what's been underquoted, and is determining how future bidding will be achieved.

Mr. Schillinger addressed the group stating that SAP cannot be relied upon exclusively for determining multiple potential factors that lead to ineffective procurement procedures. He further noted that the entire process needed to be done the old fashioned way, using paper (graphs) and manual tracking. Ms. Mitchell stated that the focus should cover "all corporate" profitability not just at the factory level. Mr. Lofthus added that we need to ensure we are pricing items correctly. Mr. Beus noted that pricing is not always the issue and that many times our overhead costs need to be reduced to be priced competitively.

Mr. Spears asked if we had considered a staff incentive program to enhance performance. Mr. Rutherford responded to this, noting that it is not as important to drive financial incentives as it is to hold people accountable and hire and promote the right people.

Ms. Garrett asked the group, “who are we talking about when we discuss behaviors, incentives, etc. – are we talking about staff or inmates as well?” Mr. Schillinger noted that inmates actually have “hands on” the products, much like employees within private sector companies/corporations.

Mr. Lofthus commented on the importance of the dual mission – Reentry program vs. Profit. Mr. Elliott added, “I and Mr. Elliott agreed it was important.”

Mr. Elliott noted that her message/story was good but questioned where the urgency was within the message. Ms. Mitchell highlighted that the urgency had been communicated in numerous ways recently through a video conference, weekly messages, and the agency’s staff webpages. Director Samuels agreed that inmates should be hearing some of the same messages staff are hearing. Additionally, he stated that all Wardens have been briefed on the urgency to support FPI. Mr. Elliott added that all stakeholders needed to hear the message, including inmates. Additionally he stated, “people follow leaders not missions.”

Directed to the McKinsey staff, Mr. Spears asked how they should proceed with hiring a Chief Transformation Officer. Mr. Rutherford recommended that this position be filled from the private sector for a period not to exceed two years. He added that this individual should be business-minded and capable of making an impact, as the next six months will be a strong indicator of progress. Mr. Spears asked Mr. Rutherford where we were with considering potential candidates. Mr. Rutherford stated that McKinsey would not get involved in this process unless they were certain it would help, adding that the costs associated had not been estimated.

The Board convened into an executive session.

V. Chief Operating Officer’s Report:

Ms. Mitchell thanked Mr. Lofthus and his staff for hosting the meeting and everyone else for their time and willingness to attend. She also thanked Director Samuels and the Board members for their continued support of FPI.

Ms. Mitchell supported Mr. Beus’ previous comments about FPI’s continued efforts to seek opportunities for overcoming obstacles that continually present themselves.

Ms. Mitchell reported that the Electronics Business Group (EGB) experienced a loss of $182,000 year-to-date at the factory level for FY2015. EBG is performing better than the forecasted loss of $3.3 million, and better than the same period last fiscal year ($7.5 million loss).

Ms. Mitchell further added that factories are operating at $3.8 million below plan overhead levels for the year, with better than forecasted sales ($101 million versus $58 million). Although sales exceeded plan by $43 million dollars, the group did not realize a significant improvement in earnings.

Ms. Mitchell noted that the largest contributing factors to this phenomenon are material costs (driven by new vehicles) and high factory labor rates, resulting in cost of sales of 100.1% of the selling price. EBG forecasted 4th Quarter sales and earnings at projected sales of $24,985 and projected earnings at -$2,186.

Ms. Mitchell highlighted that factory mothballing has resulted in savings of $3.4 million year-to-date for EBG. We anticipate further savings of $915,000 for the remainder of FY15.

A solicitation has been posted for bids to move the helmet manufacturing equipment from FCC Beaumont to FCI Williamsburg. Site visits will be conducted for interested contractors during the week of September 14, 2015.

Ms. Mitchell advised that contract manufacturing for solar panels has seen a marked improvement in module output since May. Panel production has doubled as a result of an improved supply chain. Our partner has acquired additional equipment that they intend to install at the FCI Sheridan factory, which should increase output by an additional 33%.

Ms. Mitchell noted that the AFFECT grant project has been slowed, due in large part to one of the utilities requiring that we fund the upgrade of a set of regulators before they will approve the interconnection agreement. We have recently received the quote for the work, and are starting the contracting process.

Ms. Mitchell stated that a contract is being negotiated with a company to produce their patented portable, deployable shelters. If this contract is secured, it will bring a significant product into our portfolio. There is a high level of interest from military commands, and more potential exists with the Federal Emergency Management Agency and Foreign Military Sales.

Ms. Mitchell noted that the Office Furniture Group (OFG) started the fiscal year strong, and is having a good year thus far through July. Sales are at 25% above plan, and the OFG factories have generated earnings of $2.9 million through July, which is a substantial improvement over the planned loss of $32,000.

Ms. Mitchell noted that sales for the seating factories have been particularly strong through the first ten months, with all factories above plan and revenue at 50% above plan. This additional revenue has placed the seating factories above their break-even points resulting in substantially improved earnings. This is directly attributed to the mothballing of two seating factories (FCC Florence and FCI Schuylkill Upholstery).

Ms. Mitchell added that the case goods factories at FCC Allenwood and FCI Ashland are also off to a strong start with sales 66% above plan. At this point, case goods earnings were projected at a $1.2 million loss, but sit at a $293,000 profit. Since the initial launch of the new laminate case goods line, Integrate, we have received $546,000 in orders. This is greater than expected, and has not had a negative impact on any other lines.

Ms. Mitchell noted that the systems furniture component of OFG is operating close to the planned level through the first ten months, and sales are 3.4% below plan of $32 million. All systems furniture production has been successfully transitioned to FCI Schuylkill. On a positive note, the mothballing of one of the systems factories has a direct cost savings impact on the overall systems furniture program.

Ms. Mitchell spoke of four locations in mothball status - FCC Coleman, FCC Forrest City, FCC Florence, and FCI Schuylkill (Upholstery). The overhead savings year to date for mothballed locations is $3.9 million.

Ms. Mitchell noted that the metals component of OFG is operating close to plan for the first ten months with strong sales at FCI El Reno being offset by a slower start at FCI Terminal Island. Although the metals product group is recognizing a profit, the metals product line is producing lower than anticipated earnings due to the losses recognized at FCI Terminal Island.

Ms. Mitchell highlighted that OFG continues to benefit from the repatriation authority through the manufacturing of wooden games and hospitality seating. Both of these programs are at FCC Allenwood. Ms. Mitchell added that FPI is also evaluating manufacturing sewing machine cabinets at FCI Ashland. This pilot was approved at the last Board meeting.

Ms. Mitchell commented that, since the last Board meeting, the U.S. Department of Veterans Affairs (VA) Medical Center in Manhattan, NY project ($500,000) was installed. It was a mix of systems furniture and Freedom task chairs. Ms. Mitchell added that the VA was very pleased with the “great job” UNICOR did on the project as a whole from design, manufacturing, project management and installation.

Ms. Mitchell advised the Board that this is the first work UNICOR has done for the VA in Manhattan but not for the VA as a whole. There is potential for more work to come from VA Manhattan. The VA as a whole has the potential to become a large house account. This project was significant, due to the fact we have been trying for years to get the VA to purchase more from UNICOR.

Ms. Mitchell noted that due to the financial uncertainty of the Government in FY16, OFG expects revenue for FY16 to be about 31% below the FY15 level. The decrease is spread equally among the four furniture components – case goods, seating, systems furniture and metals. Though the federal market continues its steep decline, OFG has successfully grown its share of the shrinking market. This has enabled the group to greatly reduce the impact of the federal spending reductions. Additionally, the mothballed factories continue to have a significant impact on the bottom line.

Ms. Mitchell noted that the Recycling Business Group (RBG) has performed well during this year with a stronger than planned 1st Quarter but has fallen short in the 2nd and 3rd Quarters. In relation to its year-to-date targets, RBG is 3% below sales plan and 11% below earnings plan when delayed shipments from the General Services Administration (GSA) were realized. The delays from GSA were the result of its warehouse consolidation initiative.

Ms. Mitchell noted that the greatest impact upon the group’s performance is the significant drop in the commodity markets which directly impacts the majority of RBG’s revenue from scrap sales. Commodity prices have dropped an average of 20% in the last year (July 2014-July 2015), including gold at –16%, aluminum at –17%, and copper at –25%. To help offset this impact, RBG is proactively seeking to increase their volume and break down additional materials. While this helps reach the revenue target, it comes with a higher price, i.e. more labor to process, more shipping fees and more material to purchase. As a result, RBG’s earnings are a smaller percentage of its sales.

Ms. Mitchell added that RBG projects to end the fiscal year approximately 6% below sales plan and 15% below earnings plan. Though below plan, RBG anticipates finishing the year with more than $5.2 million in earnings. Ms. Mitchell interjected thanks to Mr. Lofthus for his memo encouraging all Heads of Departments to support RBG’s electronics recycling program. The White House Council on Environmental Quality lists UNICOR’s recycling program as the first option to be utilized by the Federal Government when disposing of excess electronic equipment.

Ms. Mitchell noted that RBG projects a decrease in revenue of 5% in FY16. RBG expects to increase its volume by 15%, but that will not be enough to counter the 20% drop in commodity prices. Several global factors have pushed commodity prices down, and virtually all industry analysts expect prices to remain low during FY16. To help offset the dramatically lower commodity prices, RBG activated its newest collection center at the Metropolitan Detention Center (MDC), Brooklyn, NY in June. The MDC Brooklyn collection center will send material to RBG's factory at FCI Fort Dix, providing additional material to eventually allow the Fort Dix operation to expand. Additionally, RBG plans to expand their collection efforts in the Seattle/Tacoma area which will supplement the United States Penitentiary (USP) Atwater operation.

Mr. Gale noted that the next facility visit by the Board should involve a factory operation with a diverse and important mission. Ms. Mitchell responded by stating that every operation is important. Mr. Gale concurred and stated that "importance" was not the issue; FCI El Reno was a good visit because of its diversity in operations. He further recommended that the Board observe factories/operations that could spark creativity. Ms. Mitchell noted that factories previously visited were very diverse and when considering future tours, driving distances were taken into account which eliminated some of the more diverse operations, such as FCI Tallahassee.

Ms. Mitchell added that RBG's factory margin is expected to drop from the FY15 level of approximately 29%. This margin, while still strong, is a direct result of the commodity price drop as well as increased competition from private sector companies. Competition from private sector recyclers is now forcing the group to purchase material that used to be acquired for free from some of its customers. These costs reduce RBG's margin but are necessary to remain competitive.

Ms. Mitchell highlighted that RBG is currently working on two technical proposals and plan to bid at a cost per pound solicitation, one for facilities east of the Mississippi and one for facilities west of the Mississippi. This is an extensive undertaking and would provide approximately double the material that we currently process yearly. A part of the solicitation is providing demilitarization (demil) services (destruction) for certain materials. One certified demil location is required for each contract. RBG does have experience in performing demil services. The Defense Logistics Agency will ship all material and we will pay them per pound if we win the bid. The technical proposals (one for each solicitation East/West) are due September 17, 2015.

Ms. Mitchell advised that RBG is continuing to diversify its operations into other areas such as testing, sorting and recycling items such as small electric heaters, push mowers and string trimmers in an effort to increase its business with non-federal customers. This departure from RBG's standard electronics processing increases its ability to employ inmates, while expanding its market share among private sector customers. These operations have much smaller margins than electronics recycling, but are still a desirable market for several RBG private sector customers.

Ms. Mitchell added that RBG also benefits by enhancing the revenue of a larger factory operation, which helps to cover fixed costs, and RBG has seen an increased interest in its electronics recycling services from several county and municipal governments. RBG continues to seek opportunities in which it can offer strategic advantages over its competition.

Ms. Mitchell noted that the Services Business Group (SBG) has generated strong revenues through the first ten months of FY15, $28.6 million versus a plan of $27.3 million, which is 5.08% above plan. SBG planned for earnings of $1.6 million but actual earnings were $4.1 million, which is 169% above plan.

Ms. Mitchell advised that SBG's planned overhead was $15.2 million, with actual overhead of $14.2 million, which is 6.11% below plan. The positive variances in sales and earnings are due almost entirely to the three print plants at USP Leavenworth, FCC Petersburg and FCI Sandstone. However, SBG also had higher than planned positive earnings year-to-date at our Filters Plant and our Data Plant.

Ms. Mitchell noted that call center at both FPC Bryan and FCI Dublin have had positive earnings year-to-date; however, the loss of a key contract at FCI Tallahassee has resulted in a loss for this component. That contract was terminated by FPI due to the failure of the customer to provide sufficient work to sustain the factory.

However, SBG was successful with a re-launch of FCI Tallahassee with four staff brought out of mothball status in the 4th Quarter. SBG plans to employ up to 120 inmates at FCI Tallahassee next fiscal year. SBG's call center program is expected to close out FY15 with positive earnings in the 4th Quarter.

Ms. Mitchell reported that staff and inmate training continues on the Virtual Switch project. The BOP Reentry Division staff are writing the script for ex-offender questions for this project, which SBG is hoping to implement sometime toward the end of the 1st Quarter of FY16. New Business Development is also preparing sales brochures/information for this project and SBG has two other potential customers interested in this technology.

Ms. Mitchell noted that SBG's distribution program has increased volume, and SBG favorably negotiated pricing in its hanger sorting operation at FCC Petersburg and is expected to meet projected earnings for FY15.

Ms. Mitchell added that FPI had launched the Commissary distribution program at the FCC Lompoc Facility with prepackaged food items and plans to sell instant coffee to the Western Region institutions late in the 4th Quarter.

Ms. Mitchell noted that the box project that was approved at the last Board meeting has activated two locations in FY15, FCC Coleman and FCI Fort Dix, and we expect positive sales for both locations in FY16. FPI is also preparing to launch additional locations possibly at FCC Florence, FCC Victorville and USP Atlanta.

Ms. Mitchell advised that the Print Plants are on track to exceed planned earnings in the 4th Quarter. Signage Plants are down and are expected to end the year lower than planned in sales and earnings. Although business has picked up during the 4th Quarter in both sign factories, we still anticipate ending this year with lower than planned earnings by approximately $350,000.

Ms. Mitchell stated that FPI recently terminated its two promotional products contracts as they have not been profitable for the last three years. This became more evident this year at FCI Cumberland as this product line comprised the majority of their business. Although we will not be making "trinkets" at this time, we will continue to make awards.

Ms. Mitchell expressed that FPI hopes to replace the loss of the promotional products business with the Commissary prepackaged work for the immediate future and also reevaluate the work load for signage work at both locations in 2016.

Ms. Mitchell noted that the filter program will end the year above planned sales and earnings. Year to date, the filter program is above planned sales by $818,000 and above planned earnings by $191,000. Data and computer-aided design (CAD) operations sales are 5% above plan and earnings are 68% above plan. We anticipate finishing well above plan for FY15. This is due to a large backlog of work earlier this year, which we have now worked through. We expect a slight increase in FY16 in this program.

Ms. Mitchell added that SBG has employed an average of 14 repatriation inmates at our FCI Cumberland Signage Plant year to date.

Ms. Mitchell advised that SBG mothballed FCI Tallahassee this fiscal year for four months and had a savings of $188,372. FPI realized $221,000 in overhead savings at our three Print Plants through July of this year. SBG expects revenue for FY16 to be 29% above the FY15 level. The group anticipates sales and earnings from its existing customers and newly reactivated FCI Tallahassee call center the box distribution project; and Commissary sales.

Ms. Mitchell noted that through ten months of FY15, revenue for the Clothing and Textiles Group (CTG) was above plan by 15.6% ($139 million vs. $120 million). Earnings were 25% above plan ($10.8 million vs. $8.7 million). The significant increase in earnings is due to increased production, which was spread among all product lines.

The group is projecting an additional $41.5 million in sales and $5.9 million in earnings for the remainder of the fiscal year. Based upon these projections the group should finish the fiscal year with approximately $180.7 million in sales and $16.7 million in earnings. This equates to an 8.7% increase in sales and a 48.5% increase in earnings compared to FY14. Factory overhead is 7.3% above plan or $3.0 million. This was mostly due to the increase in inmate payroll, new minor equipment purchases and repairs of existing equipment attributed to the increase in production.

Ms. Mitchell stated that CTG is projecting sales of $153.6 million and earnings of $6.17 million for FY16. These projections are based upon the anticipated reduction in sales and selling prices for some of our most profitable products. We are expecting a reduction of sales for our Outer Tactical Vests from approximately $24.0 million in FY15 to just over $11.0 million in FY16. Our second highest impact on earnings for FY16 is due to the reductions in selling prices recognized for existing products such as ACUs.

Ms. Mitchell noted that several customer contracts have expired or are due for renewal. With the 5% rule now in effect on Federal Stock Code 8415, CTG has to openly compete on these products. One example of the impact is the reduction in selling price for the Army Physical Fitness Uniform Trouser. The current selling price is $28.04 each. The new selling price based upon the five-year contract awarded May 15, 2015 is $20.50 each. We are projecting sales of 210,000 units in FY16. At a $7.54 per unit reduction in selling price this will have a negative net effect on earnings of almost $1.6 million.

Ms. Mitchell added that several others products to varying degrees will be affected by the bid process including one product, which currently feeds work into seven factories. If you remember, in FY 14 we were required to reduce our proposed selling price for this product by approximately 10% in order to secure the award. Additionally, FPI will implement modifications to the current method that determines inmate pay. This change will align the structure of FPI's piece rate and group rates with those in the private sector.

Specifically, the applied efficiency and personal fatigue and delay (PF&D) rates in use today artificially inflate inmate pay, while reducing actual available capacity.

Ms. Mitchell advised that inmate employment in FPI as of July 31, 2015 was 12,121 with 1,201 inmates in job share; 894 veterans; and 2,938 inmates within two years of release. Additionally, FPI currently employs 985 inmates in repatriation.

Ms. Mitchell added that there has been little change in the number of inmates employed in repatriation jobs. This is due to turnover of key New Business Development personnel and a downturn in business for certain business partners.

Ms. Mitchell noted that 48 active projects are in production or in the process of being finalized. There are 20 potential projects that are in various stages of development. Seven projects currently in production are from prior customers that were pleased with the work that had been previously done.

Ms. Mitchell stated that the cardboard box pilot that was approved has now been successfully started at FCI Fort Dix and FCC Coleman. CTG is currently working on starting the operation at FCC Florence and looking at sites for west coast and Texas operations.

Ms. Mitchell noted that during the 3rd Quarter FPI signed an agreement to remanufacture trailers and prototypes are being developed at FCI Gilmer. If successful, this project could lead to reactivation of FCI Bennettsville.

Ms. Mitchell mentioned that FPI has successfully been manufacturing cables as part of a Prison Industry Enhancement Certification Program (PIECP) since July 2014. This project is currently employing nine inmates at FCI Estill. We successfully completed our first PIECP audit in July. We are still awaiting our official results. The program continues to employ an average of five inmates.

Ms. Mitchell spoke of a company that was recently awarded a new contract that we anticipate will require inmate employment levels to increase to a total of 25 inmates. This added inmate capacity is expected to come within the next month and remain steady for approximately 48 months. Earnings were $57,000 thus far this fiscal year.

Ms. Mitchell highlighted that FPI entered into a PIECP agreement with a company to have a cutting and sewing operation at FCC Butner. Fifty-five inmates were interviewed and production began in mid-June. The program is currently employing 50 inmates.

Ms. Mitchell added that the New Business Development Group (NBD) continues to meet and negotiate with potential vendors to secure work under our new authorities. To date, 35 Contract Manufacturing Agreements (CMA) are in place, compared to 24 last year this time. In addition, there are at least 48 viable opportunities currently being pursued by NBD.

Ms. Mitchell noted that we continue to explore new opportunities, such as fire suppression systems, modular homes, and LED lights. At USP Marion, manufacturing operations have been relocated to the old Facilities area within the institution. This move has resulted in an additional 50,000 square feet of manufacturing space at USP Marion.

Ms. Mitchell explained that the institution experienced a lightning strike to one of its transformers and power availability has been limited to one-third of normal power capacity. On a positive note, the plant has been working with facilities to restore full power for the hanger operation.

Ms. Mitchell noted that we expect to be back up to full capacity by October 1st. In the mean time, we are currently employing 25 inmates to prepare the machinery and install the necessary light guards for safety purposes. We are planning to employ a minimum of 60 inmates over two shifts beginning October 1st. That number is expected to grow to approximately 75 inmates in the near future.

Ms. Mitchell highlighted that Agribusiness continues to be profitable. An environmental evaluation was conducted, and a draft statement of work is in process for the design/build of a dairy in California. Ms. Mitchell noted contacts with other agencies who we could supply milk to include possible private prisons in California. We are currently exploring expanding dairy farming operations to beyond FCC Lompoc and FCI El Reno. A business plan has been drafted and will be presented to corporate management next week regarding constructing a dairy on the east coast.

Ms. Mitchell noted that in June an agreement was entered to farm soybeans at FCC Forrest City. The crop is in the ground and this has enabled us to develop processes to possibly expand to other institutions.

Ms. Mitchell stated that FPI staff have been working with staff from the Bureau of Land Management (BLM) and institutional staff at FCC Coleman to finalize an interagency agreement related to a wild horse program.

Ms. Mitchell spoke about a number of cost saving initiatives, including:
Organization structure; shared efficiencies (what functions can BOP perform for us); Review of Product Lines/Services; Trinkets, Contracting & Procurement/Agreements; and Plans for procurement Consolidation. Other business initiatives include:
HR/Staffing Issues (sought specialized experience); Print Program Manager; Agribusiness manager; Process Improvements (launched new BOMS and Routings and conducted specialized SAP training); PF&D review, annual training plan; staff training in Production, Finance and SAP; and Aggressively Pursuing BOP Opportunities (Socks and Commissary items).

Ms. Mitchell noted that to improve services to BOP, we have increased our safety stock for several items, including commissary items and inmate clothing. T-shirt sales orders for FY15 are currently at 968,010 units and should equal or exceed FY14 totals of 1,012,568 units. Commissary sales are at 46,647 units, surpassing last year's total of 1,395 units. Orders continue to be received on a weekly basis. We anticipate a significant increase in sales once the Southeast Region begins placing orders.

Ms. Mitchell noted efforts to address and remedy some vendor issues in optics that have caused delays. We have prepared a plan to move our plastic molding operations to our optics factory to be more efficient and less reliant on vendors, and we have also taken concessions against vendors, improved quality and delivery, and have communicated our commitment to be the BOP's vendor of choice.

Ms. Mitchell spoke about efforts to continue promoting FPI:

Ms. Mitchell highlighted the national videoconference, which was held in conjunction with the union in April explain to all UNICOR staff as to where we stand, what is coming and what to expect, and what we'll need to do to turn FPI's financial situation around. Since that time, the first four of the series of eight staff communications articles were reviewed and posted, with a new one posted each week. Additional ideas are currently in the works.

Ms. Mitchell advised the Board that she created her "Change Story" and worked with the General Managers and Branch Chiefs to develop theirs.

Ms. Mitchell noted that she had spoken at both Associate Wardens' training sessions in June regarding becoming the vendor of choice.

Ms. Mitchell stressed our focus on growing repatriation and PIECP opportunities. We added a second PIECP operation at Butner and refined our process, resulting in better margins.

Ms. Mitchell spoke about developing new products and customers involving steam traps.

Ms. Mitchell spoke about FPI's product development capabilities and noted that FPI hired staff for both FCC Butner and FCC Allenwood.

Ms. Mitchell provided a Kronos update: She noted that we have not yet fully converted the inmate payroll system over at any site and are still running the prior system for actual payroll. Calculation issues related to piece rate pay, longevity and vacation pay are still being resolved. Once fully implemented, the new system is expected to generate savings of approximately $1.2 million per year.

Ms. Mitchell provided a building update: For the IEVT Division's 400 Building, work is proceeding to have the sixth floor vacated by September 30, 2015 as planned. Installation of carpet and furniture is underway. Estimated total cost for the project is $700,000 which is less than one year's rent for the vacated floor. Inmate crews from FCC Petersburg have been used to help reduce the cost of this project.

Ms. Mitchell noted that since last year, we have focused on these areas and continue in these efforts. Notably, we are seeking to bolster our New Business Development Group this year, and we have also been improving our procurement processes. Based on the business assessment, we also have been evaluating additional improvements we can make.

Ms. Mitchell addressed Mr. Elliott's questions from the previous Board meeting, regarding "what keeps you up at night?"

Ms. Mitchell noted below some of the responses she and her management team compiled:

- Significant contract uncertainty and variation in vendor prices with no end insight or stability and the need to lower prices to remain viable.

- Succession planning for the many retirements within the next year for our group as well as having the staff with the right capabilities.

- Security concerns and challenges of operating in a prison and also still being cost competitive.

- Staff morale and concern that staff will begin to lose hope. We need to be able to fully launch business opportunities, such as the BOP commissary program. Our positive financial position for 2016 is tied heavily to these programs at multiple factories.

Ms. Mitchell noted that FPI has recently implemented a procurement initiative to reduce our materials costs. This initiative is based upon FPI renegotiating current contract pricing and negotiating better pricing on future contracts. The group has realized savings on existing purchase orders of over $1.2 million and $760,000 on future orders. These savings have been factored into the FY16 plan.

Ms. Mitchell stated that we are also considering further a potential trucking/logistics cost savings project. The current contract expires in September 2016 and Ken Yeich is heading up this effort. So far, 50 possible transportation companies have been identified who are considered to be potential bidders.

Ms. Mitchell notified the Board that we are currently considering the further mothballing of up to 16 additional full or partial factories, as follows:

Ms. Mitchell noted that the plan for Clothing and Textiles was to consolidate (partial mothballing) operations at four complexes. Each location currently is staffed for two factories and will be consolidated down to operate as one factory. There will be seven additional factories mothballed in FY16 with anticipated savings of $5,653,114.

Ms. Mitchell explained that based upon future requirements, only two trouser factories can be supported. This will require two factories to be mothballed. The four factories will be evaluated through December to determine which factories to mothball. The two factories that maintain the highest levels of productivity, efficiency and quality (lowest levels of rework/scrap) will continue to operate as Army Combat Uniform (ACU) manufacturing sites.

Ms. Mitchell explained that based upon future requirements, only two ACU coat factories can be supported. This will require one additional factory to be mothballed.

The three existing factories will be evaluated through December 2015 to determine which factory to mothball. The two factories that maintain the highest levels of productivity, efficiency and quality (lowest levels of rework/scrap) will continue to operate as ACU manufacturing sites.

Ms. Mitchell noted that we are currently conducting an evaluation of our three print factories to determine the proper number of factories to accommodate our capacity and projected orders. Mothball dates have not yet been determined.

Ms. Mitchell reported that the Office Furniture Group (OFG) is planning to reduce the number of metal factories from three factories to two factories. We have conducted site visits to analyze capacities and capabilities of each metal factory and have determined we can mothball FCI Terminal Island and consolidate the work into FCI Milan and FCI El Reno. Anticipated savings for FY16 are $1.6 million.

Ms. Mitchell noted that due to cable orders projecting to remain flat for FY16, with no significant improvement projected, we have reevaluated our existing capacity, and recommend further mothballing and consolidation of orders. We are recommending the mothballing of FMC Lexington, pending the completion of all open orders. We are also recommending the full mothball of FCI Fairton, as plastic product orders will not sustain the factory. These moves are anticipated to save $1.7 million in FY16.

Ms. Mitchell expressed that we are taking all of the measures into consideration and baring any unforeseen issues such as sequestration, we are confident that we will be positioned to break even at the end of 2016.

Ms. Mitchell expressed thanks to the staff who have worked tirelessly over the last year to help move the initiatives forward.

Mr. Lofthus asked why potential profit was included in the proposal for socks.

Mr. Spears asked how many inmates the proposed cutting and sewing operation would employ. Ms. Mitchell stated it would employ ten inmates in repatriation work (cutting and sewing, not knitting and darning). Mr. Elliott asked if we could operate at a lower margin as opposed to a higher margin. Ms. Mitchell stated that consideration had been given to solutions such as moving operations from one location to another. Mr. Lofthus noted his concerns about forecasted “low” profits and not taking into consideration any contingency plans in the event of failure. He added by noting his concerns that there was no cushion for unexpected blips.

Ms. Mitchell stressed the fact that items such as socks are sold to the BOP and will continue to result in profits.

Action Item: Socks as a New Product

The discussion ensued on the manufacture of socks. The focus was on the very small projected profit margin of $20,000 for this venture. Mr. Lofthus expressed his concern that if one unforeseen event went the wrong way that the profit margin would be wiped out. Further discussion ensued as to how FPI costs its products. A question was raised about the purchase of equipment necessary to undertake this venture. The Board eventually approved this venture, with one vote against.

Chairman Spears provided final comments to include his appreciation to Director Samuels, Ms. Mitchell, staff present and to the Board Members for their participation in the Board Meeting.

The Board convened into an executive session.

The meeting was adjourned at 1:25 p.m.

MMitchell - acting

Mary M. Mitchell, Chief Operating Officer, Corporate Secretary